

ECONOMIC UPDATE

**LMID Advisory Group Meeting
October 23, 2008**

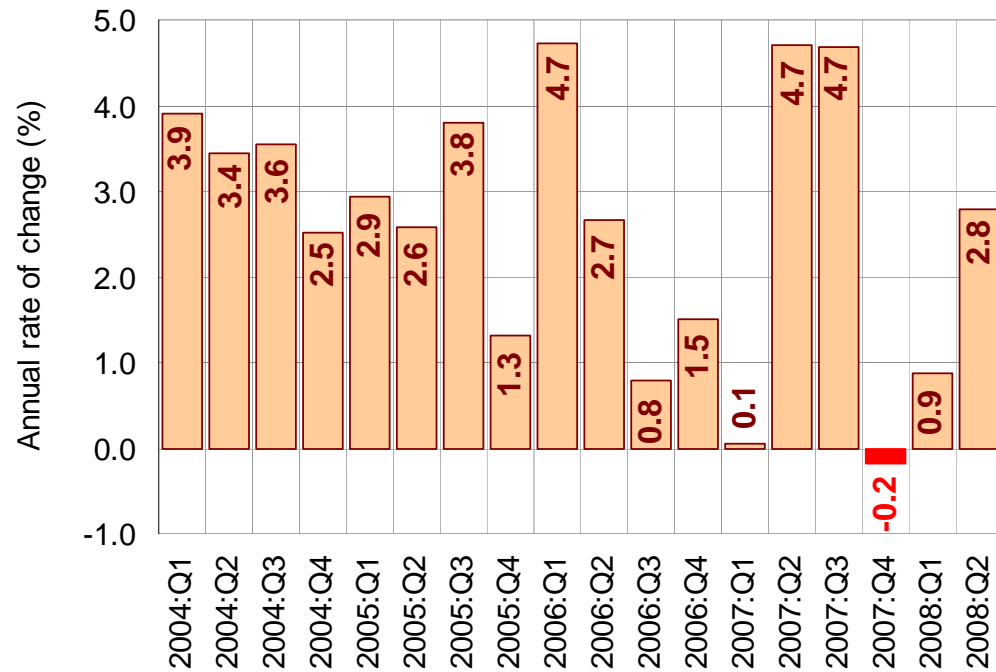
- **What is an economic recession?**

“A significant decline in economic activity spread across the economy, lasting more than a few months, normally visible in real GDP, real income, employment, industrial production, and wholesale-retail sales.”

- Determined by the National Bureau of Economic Research (NBER) Business Cycle Dating Committee, which takes an inherently retrospective approach. The Committee places considerable weight on real GDP, but a recession is more than just two consecutive quarters of negative GDP growth.
- **Growing consensus that the U.S. economy has—or is—slipping into recession that could last several quarters, and be quite severe given the financial crisis.**

U.S. Economy

**Quarterly U.S. Real Gross Domestic Product,
2004:Q1 - 2008:Q2**
(Seasonally adjusted at annual rates)

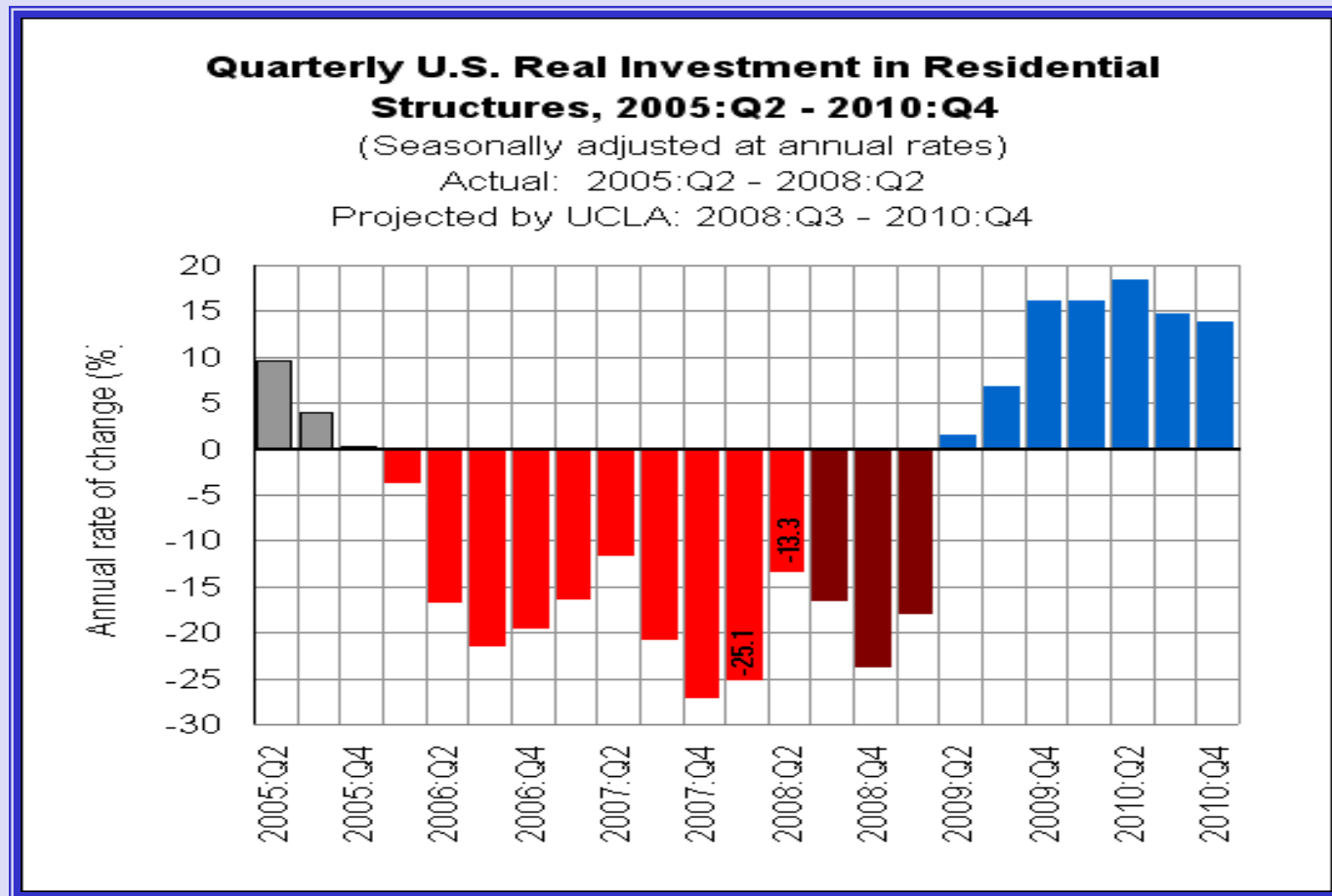


**The 2008:Q2 GDP data look quite healthy, not recessionary.
However...**

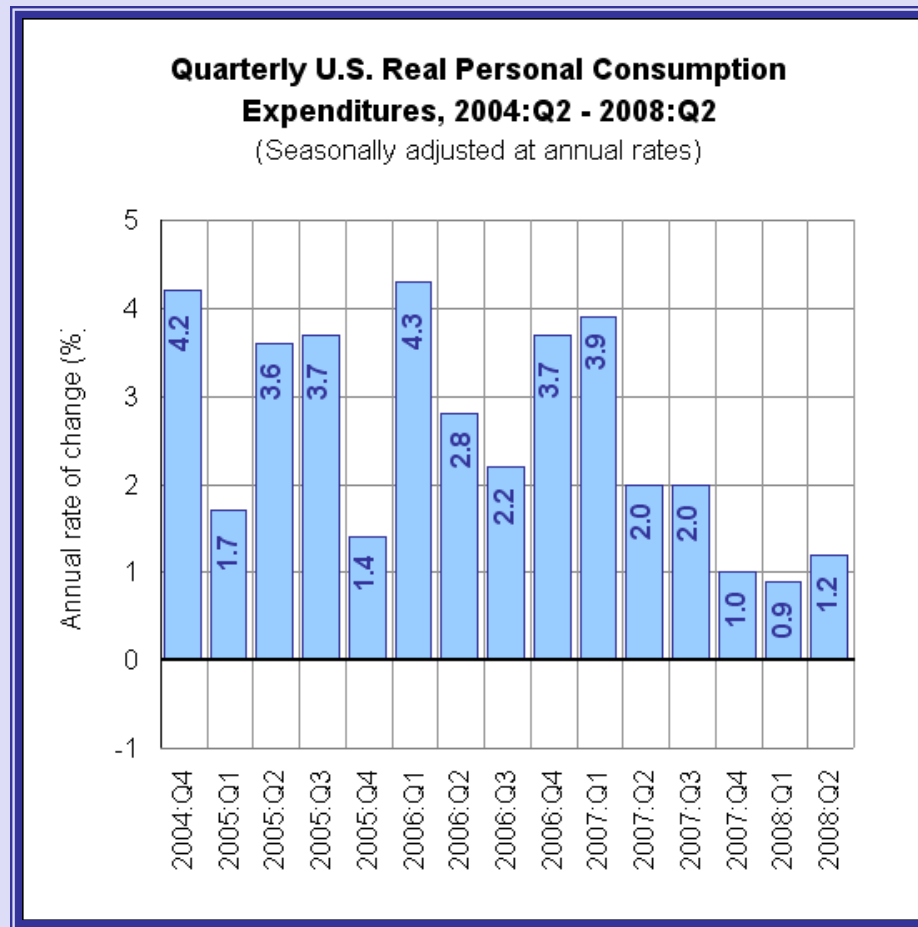
According to the U.S. Bureau of Economic Analysis, the increase in real GDP in the second quarter primarily reflected “an acceleration in exports,” a decrease in imports, “a smaller decrease in residential fixed investment, an acceleration in nonresidential structures, and an upturn in state and local government spending.”

There are real concerns that these positive contributions can not be sustained.

U.S. housing is not expected to recover until Spring 2009 at the earliest. In the meantime we are in a vicious cycle of declining home prices, more home foreclosures, scarce credit, and further uncertainty and risk in financial markets.

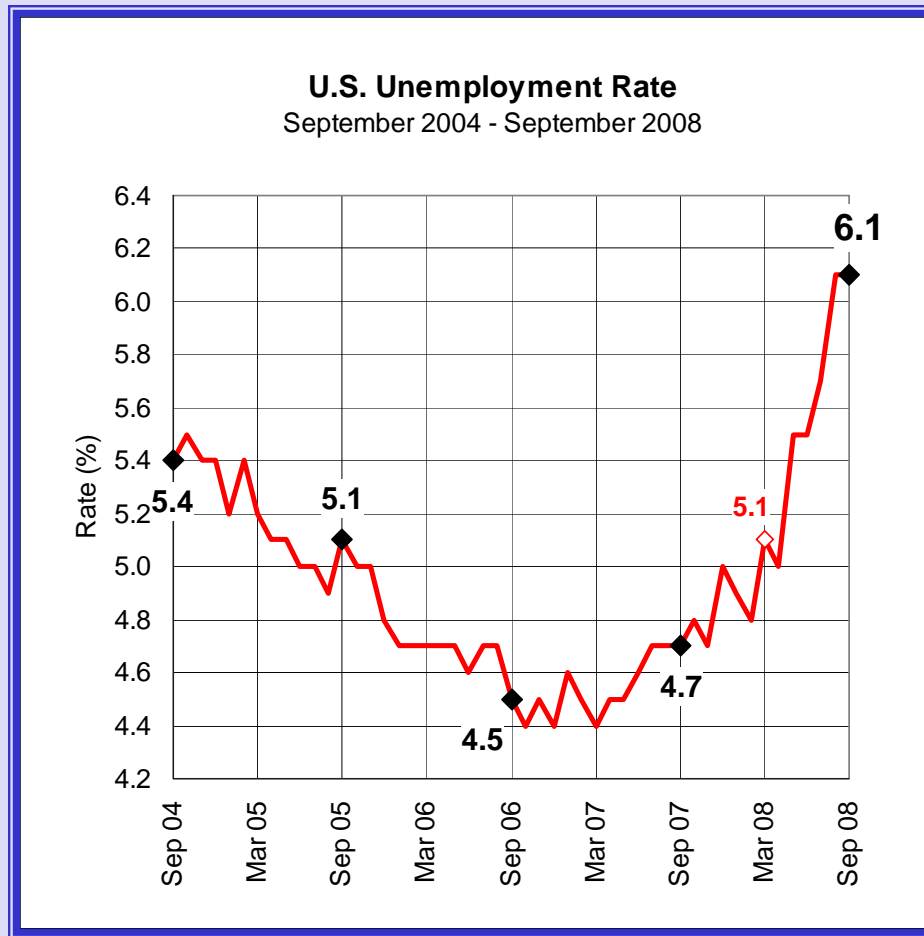


Consumer spending, the engine of the economy, has been weak for three quarters. Has the long predicted consumer pullback begun? A consumer-led recession on top of the housing and financial crisis could be severe and prolonged.



- **Decreasing U.S. imports, while beneficial for the trade balance and real GDP, reflect a slowdown in consumer spending.**
- **The housing crisis has spread to England, Ireland, and Spain; the financial crisis to much of Europe.**
- **Europe as a whole is teetering on the brink of recession. The dollar has appreciated rapidly against the Euro in recent weeks.**
- **Although exports are expected to be a bright spot in the economy, a stronger dollar and weaker global economy will likely constrain U.S. export growth rates.**
- **It is unlikely that State and local governments will spend at 2008:Q2 levels as budget cycles catch up to the housing crisis, and the Federal deficit deepens.**

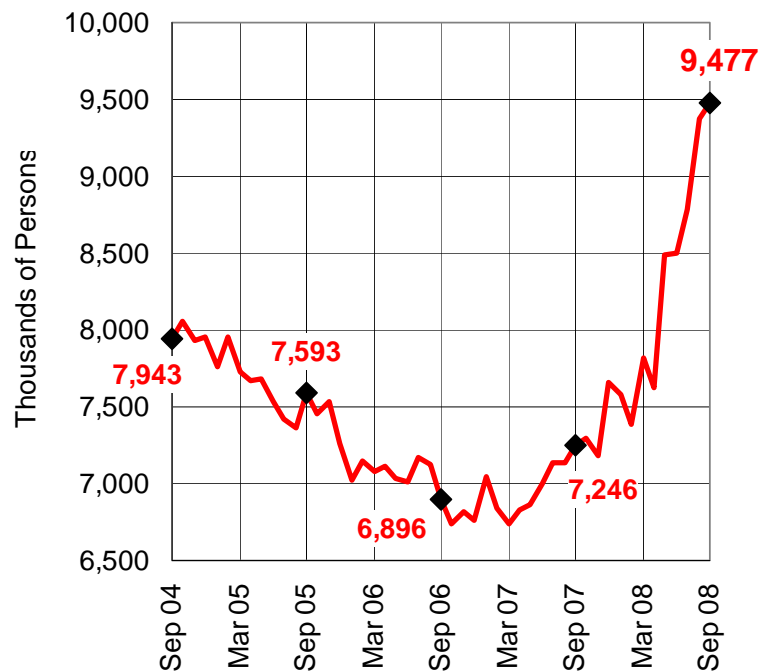
U.S. Unemployment Rate in September 2008



U.S. Civilian Unemployment

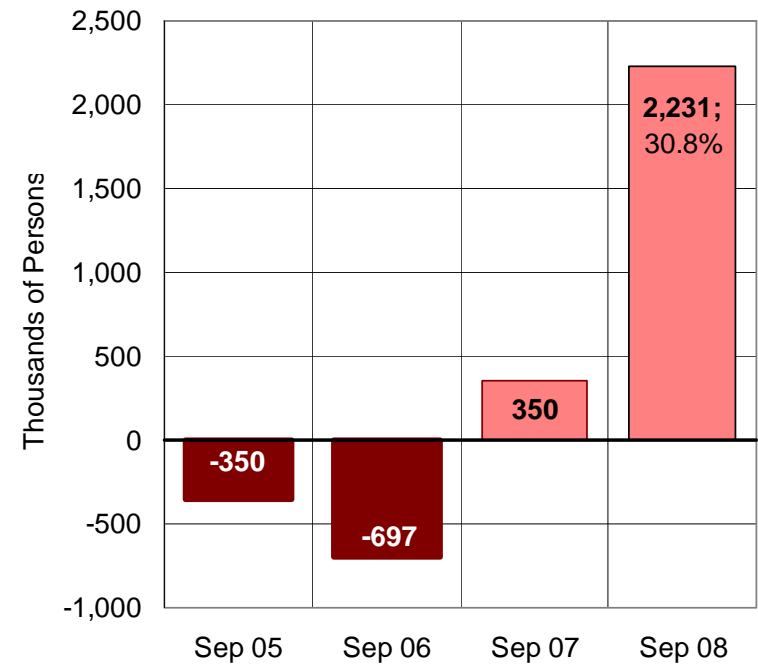
U.S. Civilian Unemployment

September 2004 - September 2008



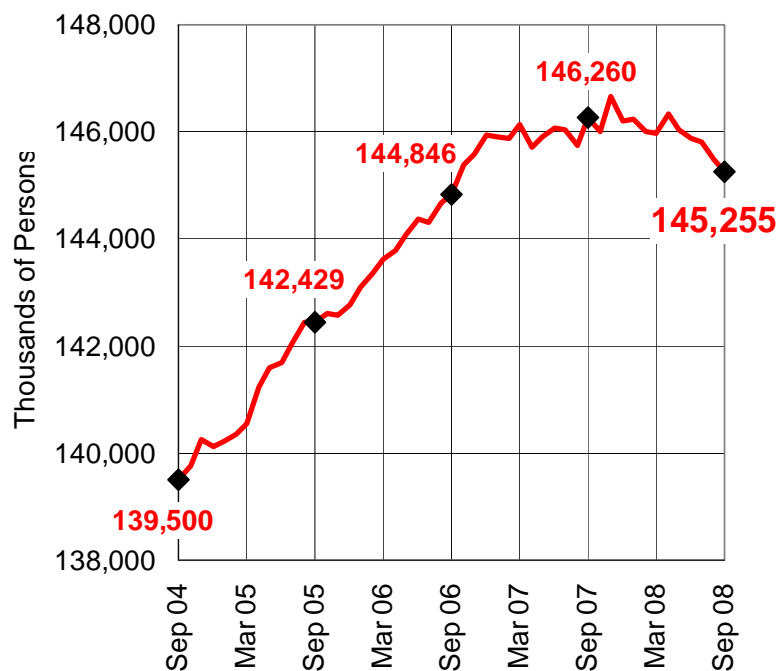
Year-Over Changes in U.S. Civilian Unemployment

September 2005 - September 2008



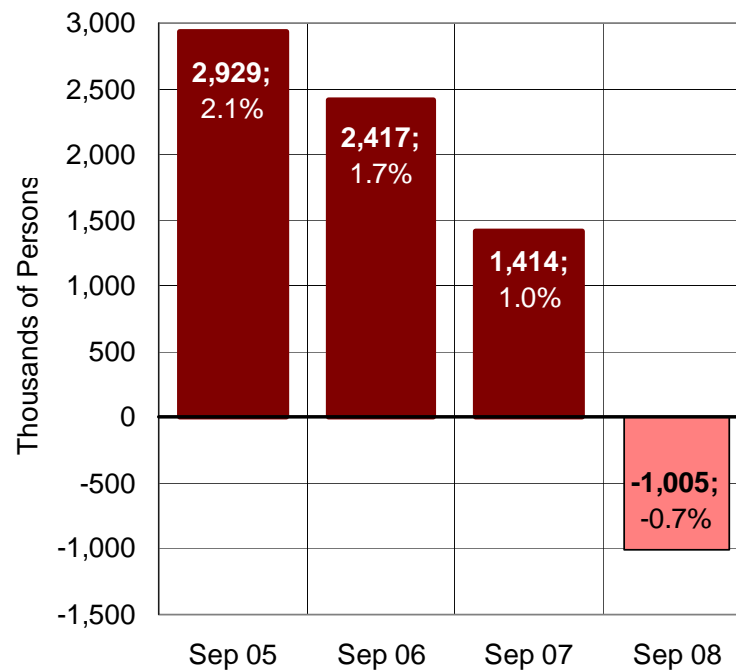
U.S. Civilian Employment

U.S. Civilian Employment
September 2004 - September 2008



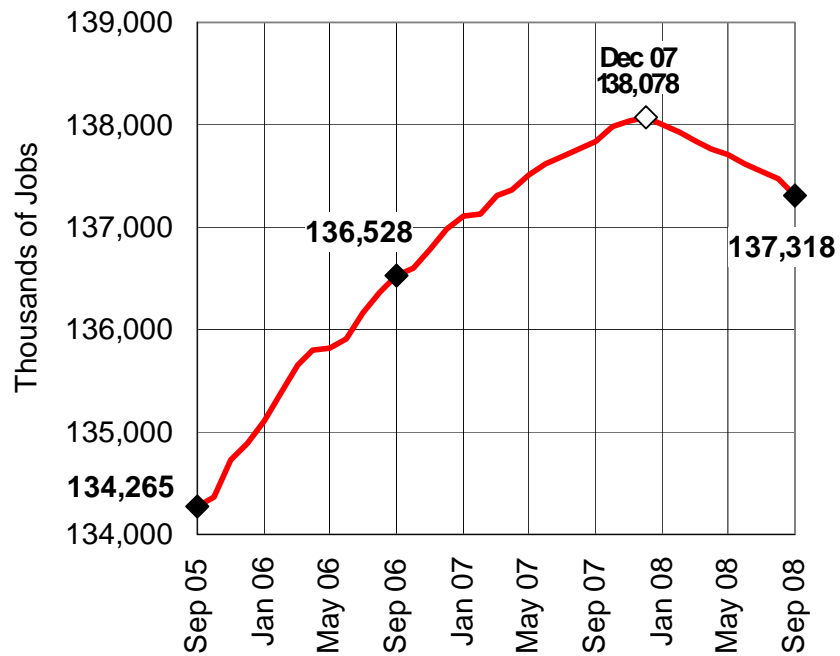
Year-Over Changes in U.S. Civilian Employment

September 2005 - September 2008

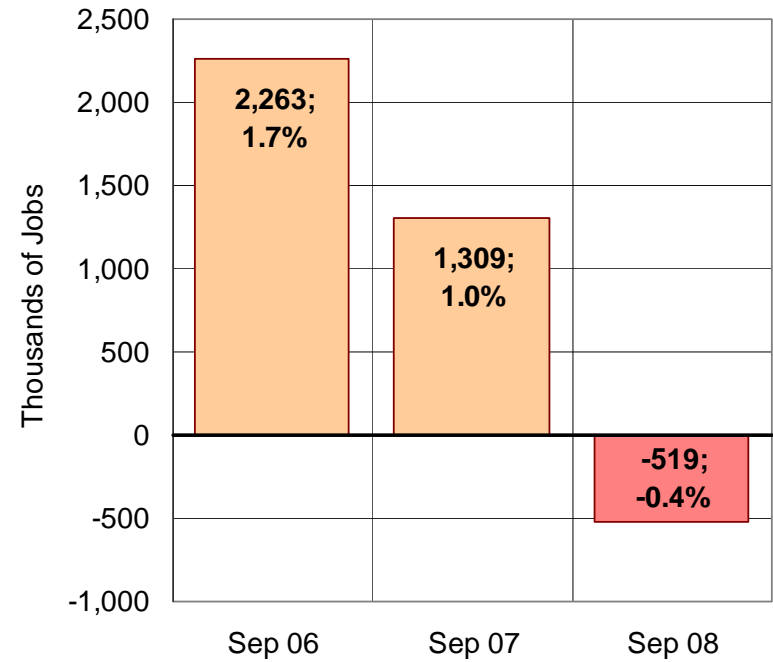


U.S. Nonfarm Payrolls

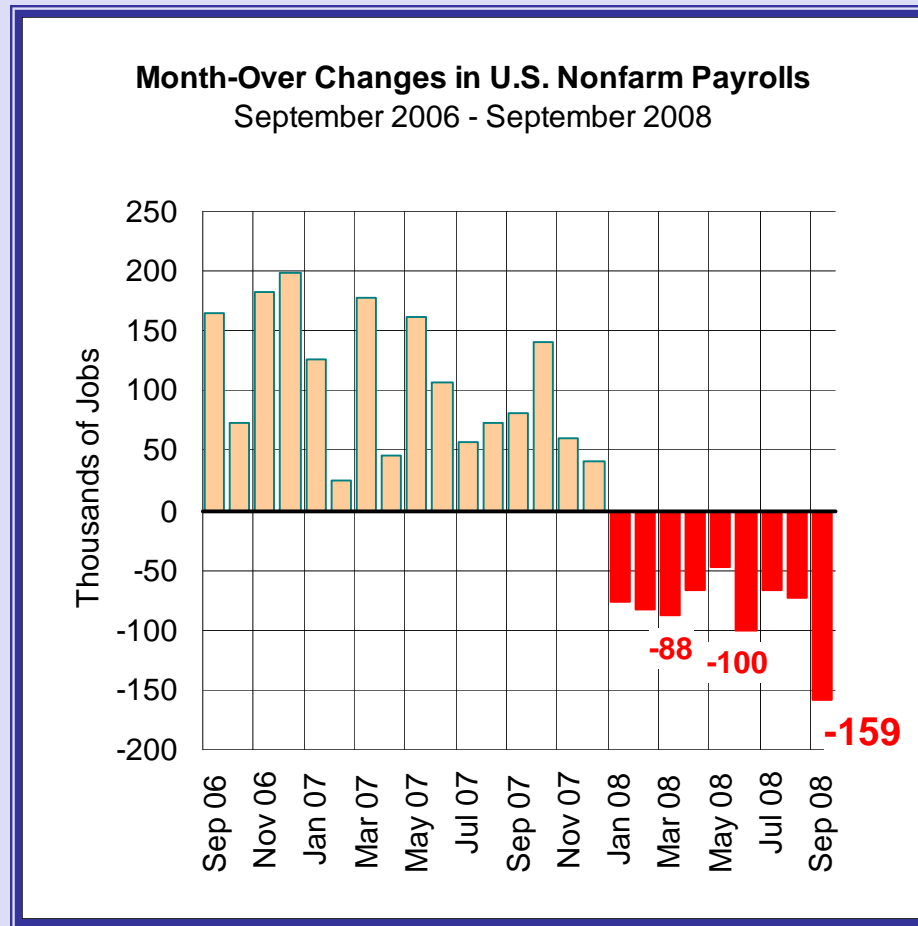
U.S. Total Nonfarm Employment
September 2005 - September 2008



Year-Over Changes in U.S. Nonfarm Payrolls
September 2006 - September 2008

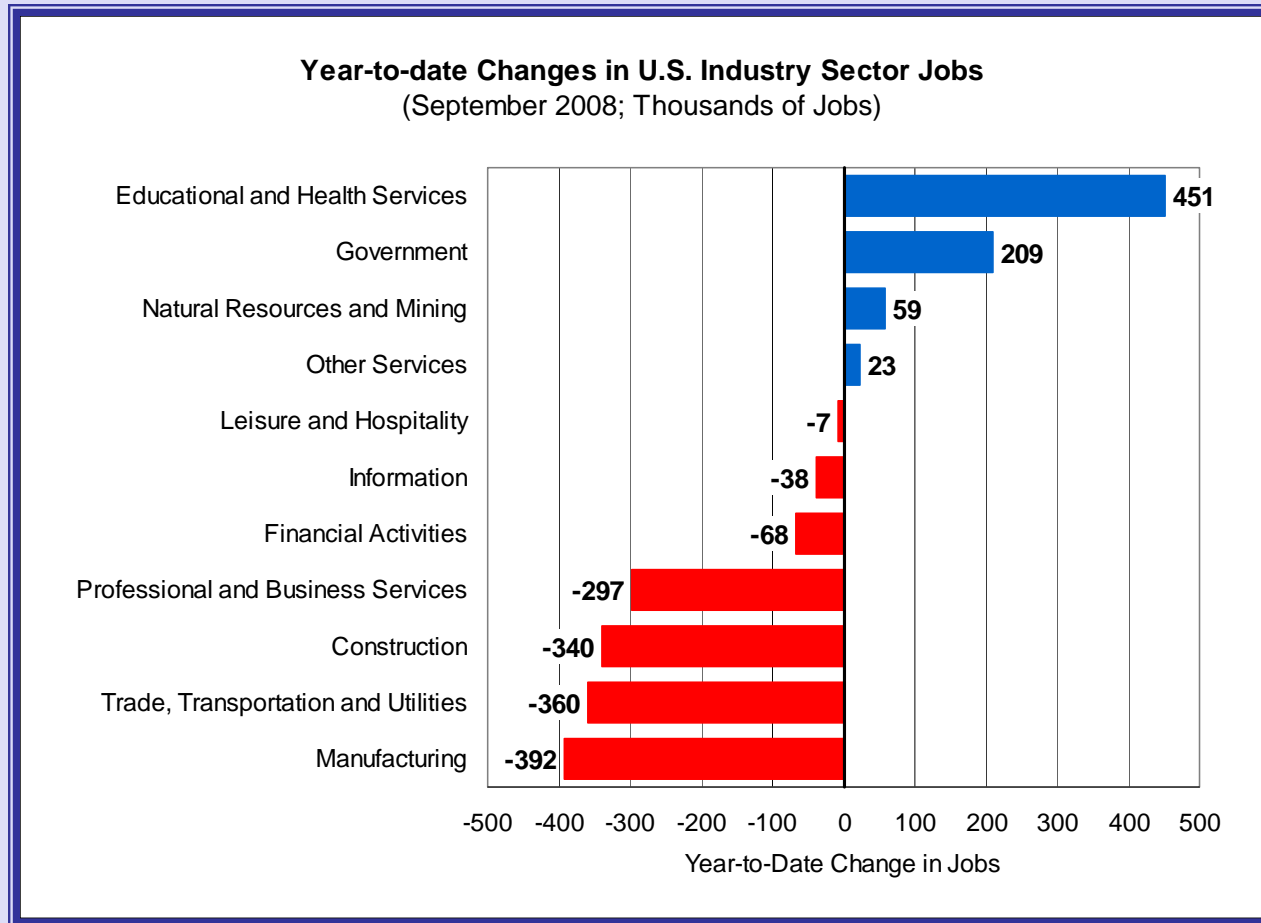


U.S. Nonfarm Payrolls (continued).



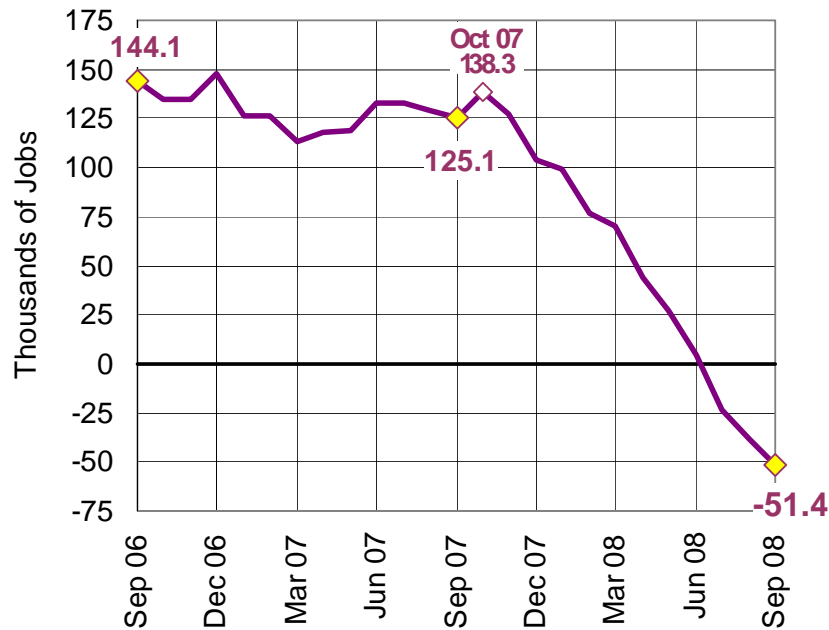
U.S. Nonfarm Payrolls

- Year-to-date in 2008, U.S. nonfarm job losses total 760,000. Seven out of 11 U.S. industry sectors have experienced job losses.

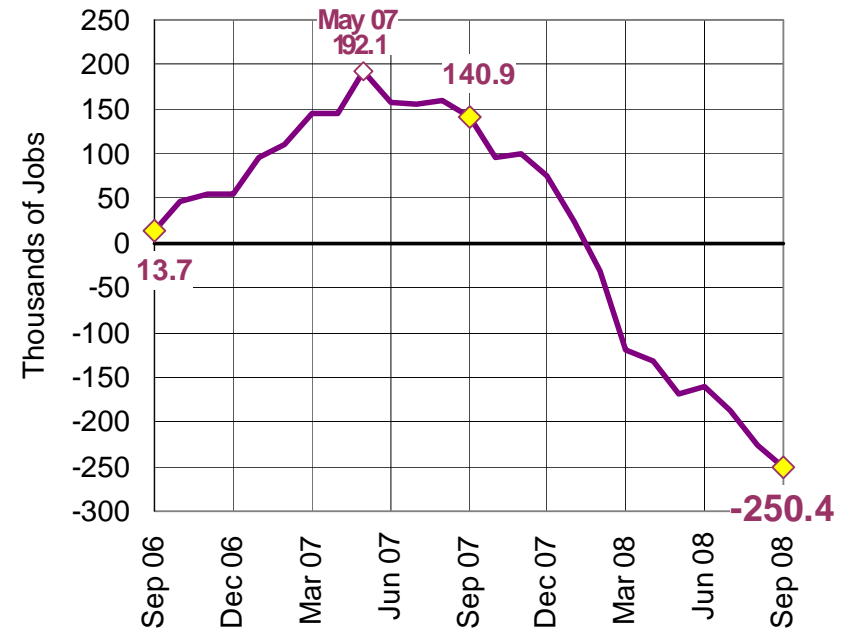


Year-Over Job Growth in U.S. Wholesale and Retail Trade

**Year-Over Changes in U.S.
Wholesale Trade Jobs**
September 2006 - September 2008



**Year-Over Changes in U.S.
Retail Trade Jobs**
September 2006 - September 2008



- The September 2008 UCLA economic forecast was not prepared to declare that the U.S. economy was in recession, although the exploding financial crisis made this outlook uncertain. Unemployment was the only economic indicator to clearly indicate that the economy was in recession.
- UCLA instead predicted that the U.S. economy would “stumble forward” as the economy undergoes “serial adjustments”: a housing market that continues to adjust, and consumers who begin to tighten their belts and save for retirement. However, the financial crisis was a major threat to this outlook.
- If the economy is in--or falls into--recession, expect economic conditions to get much worse, with:
 - * Declining industrial production
 - * More severe job losses
 - * Continuing increases in unemployment (up to 8% in the U.S., as high as 10% in CA)
 - * Further deepening of the housing crisis due to job losses.
 - * More problems in banking
 - * A lot more distressed debt

From the April 9, 2008 Economic Update

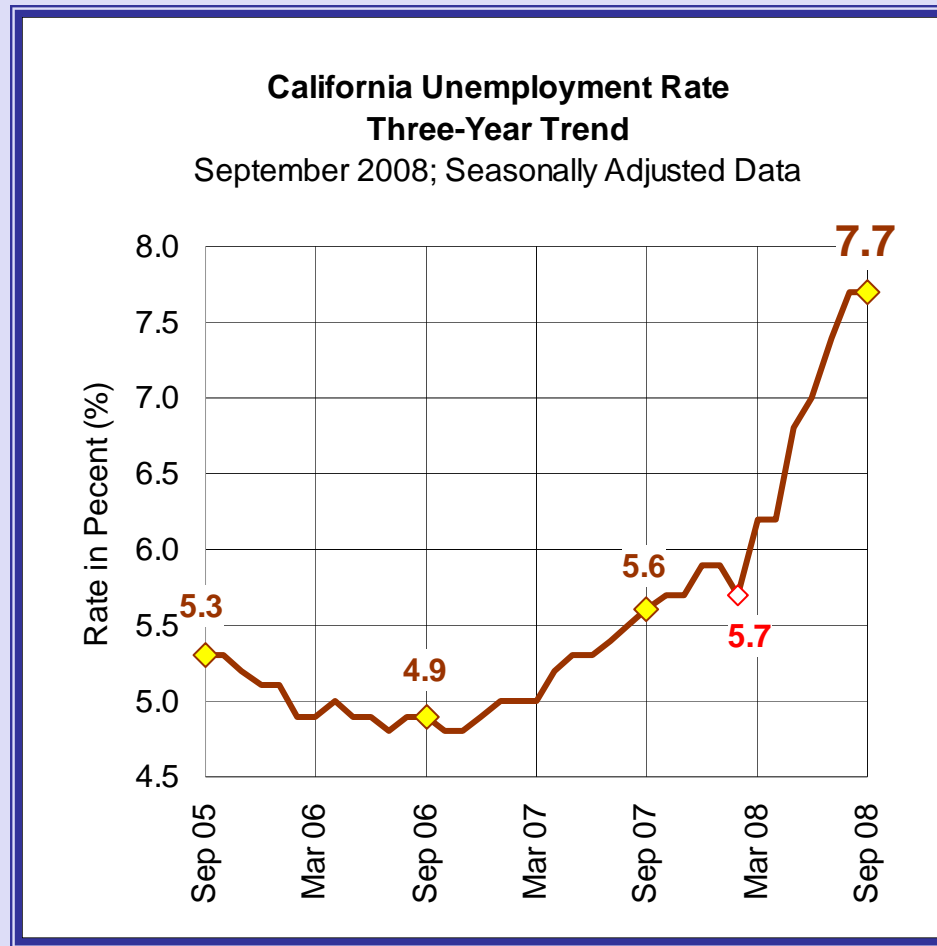
- UCLA Anderson School “clings” to idea that the current downturn will not be severe enough to meet the technical definitions of a recession, contending that “the problems in housing will largely stay in housing”. ***Indications are that the malaise is spreading.***
- At the other end of the spectrum, some economists fear we may have a prolonged and severe recession. Some even see the risk of an economic “depression”.

--These fears appear to be stoked by fears of a looming global financial crisis. Housing problems morphed into the subprime mortgage crisis which triggered a credit crunch which have created a large degree of instability in global financial markets. ***Was Bear Stearns an isolated case or the “canary in the coal mine”? NO!***

California Unemployment Rate: When Last We Spoke...

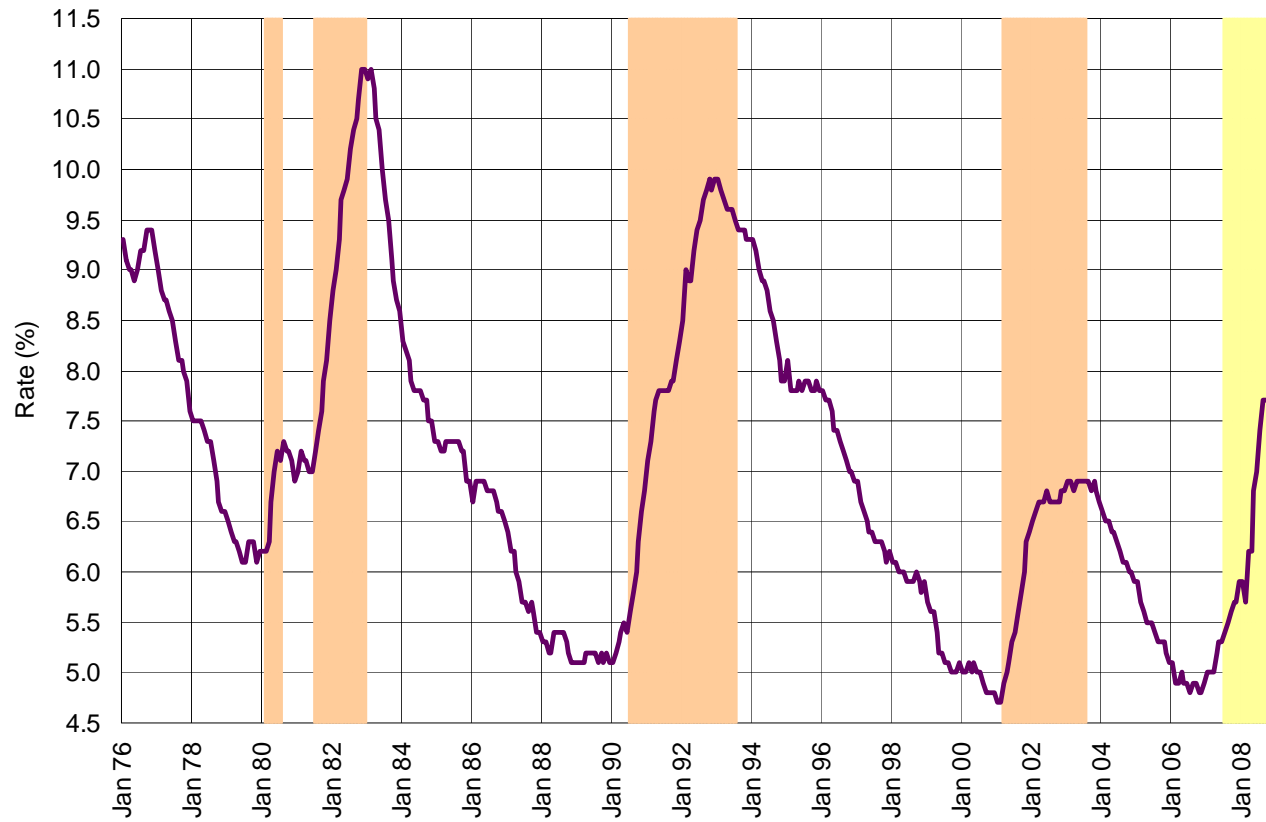


California Unemployment Rate in September 2008



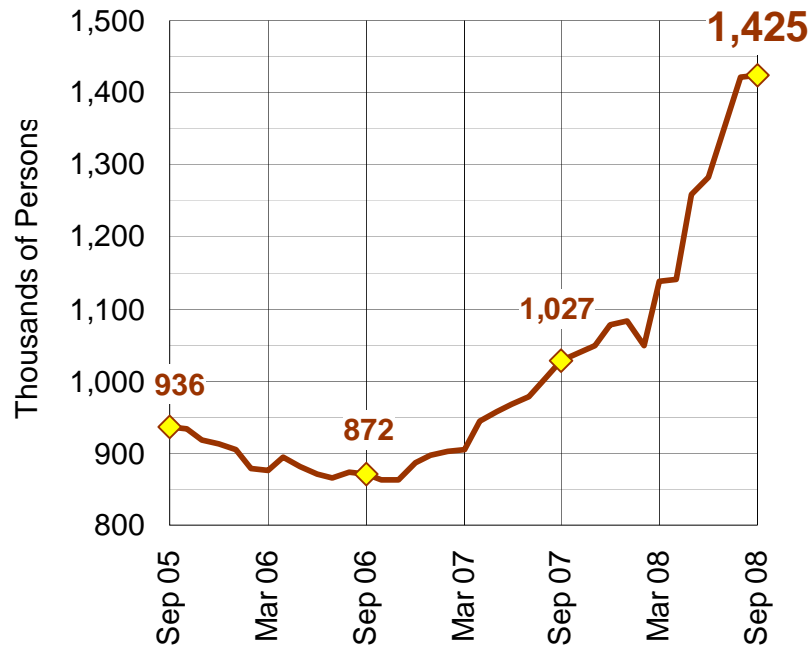
California Unemployment Rate Since 1976

September 2008; Seasonally Adjusted Data

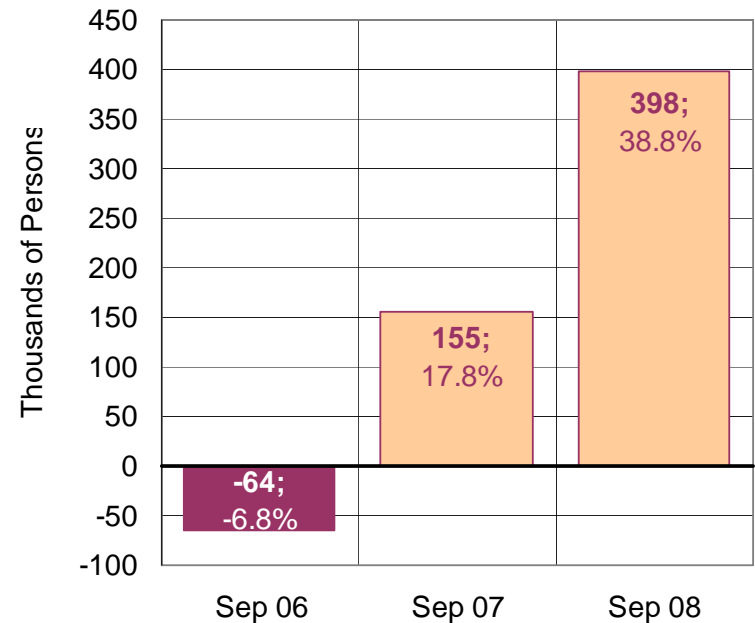


California Civilian Unemployment

**California Civilian Unemployment
Three-Year Trend**
September 2008; Seasonally Adjusted Data

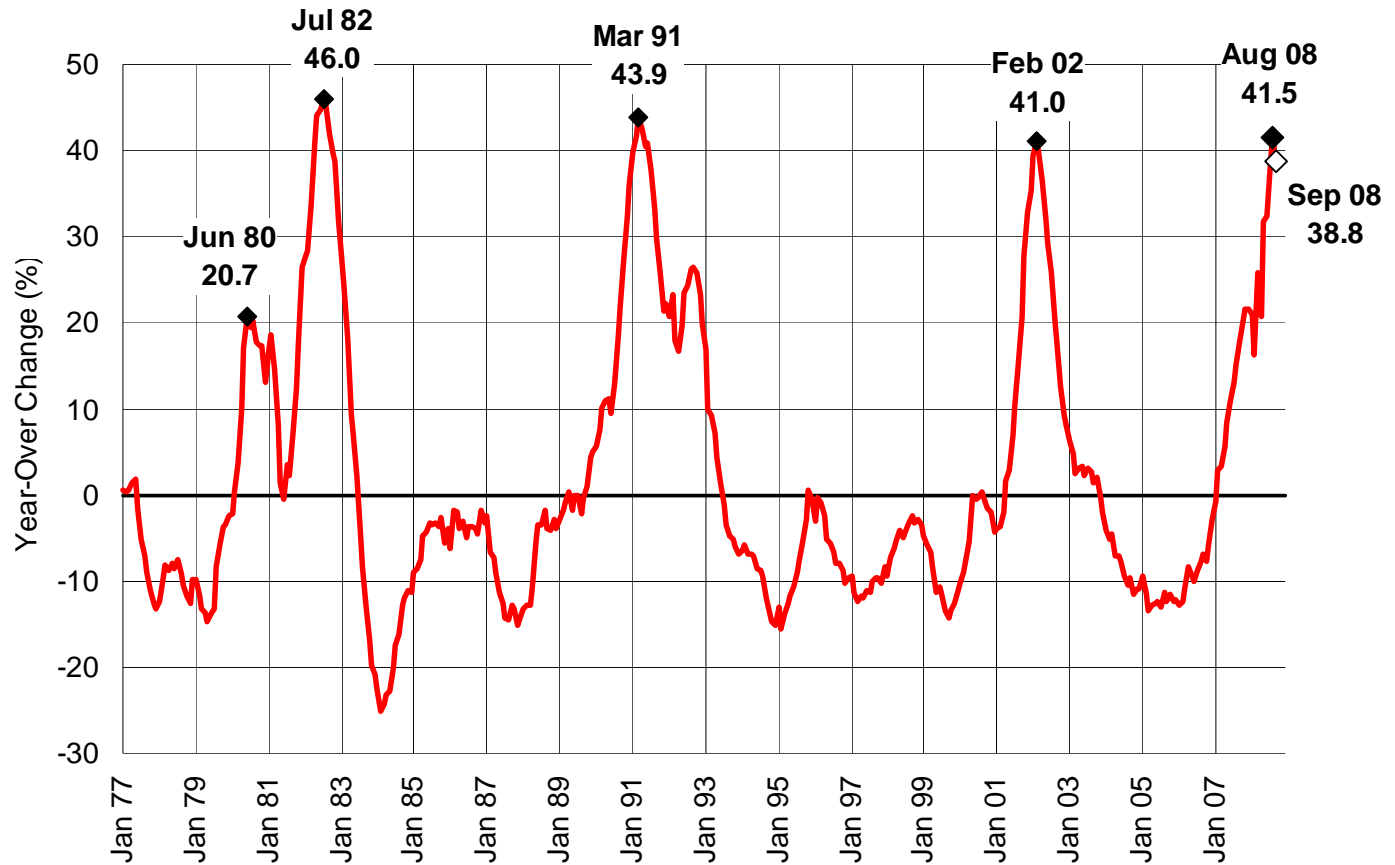


**Year-Over Changes in California
Unemployment**
September 2008; Seasonally Adjusted Data



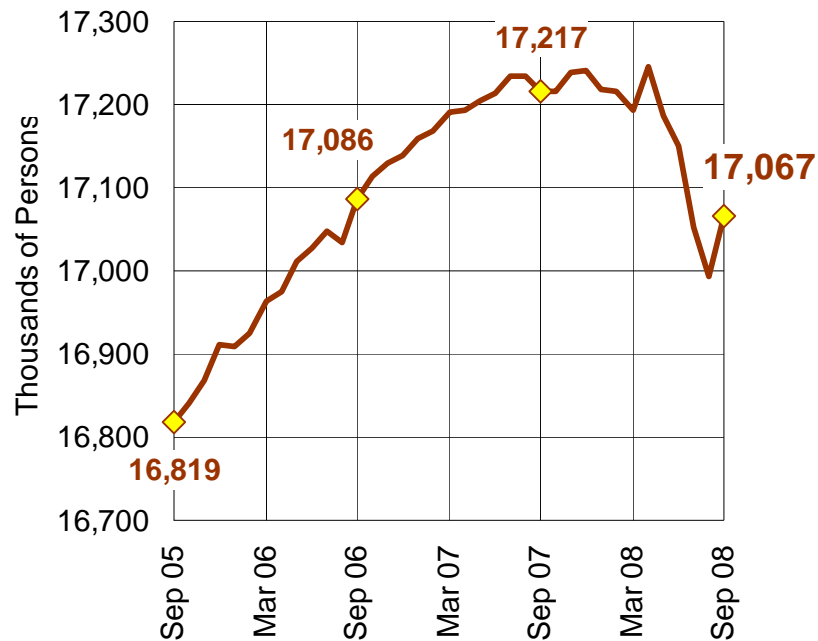
Year-Over Percentage Changes in California Unemployment Since 1977

September 2008; Seasonally Adjusted Data

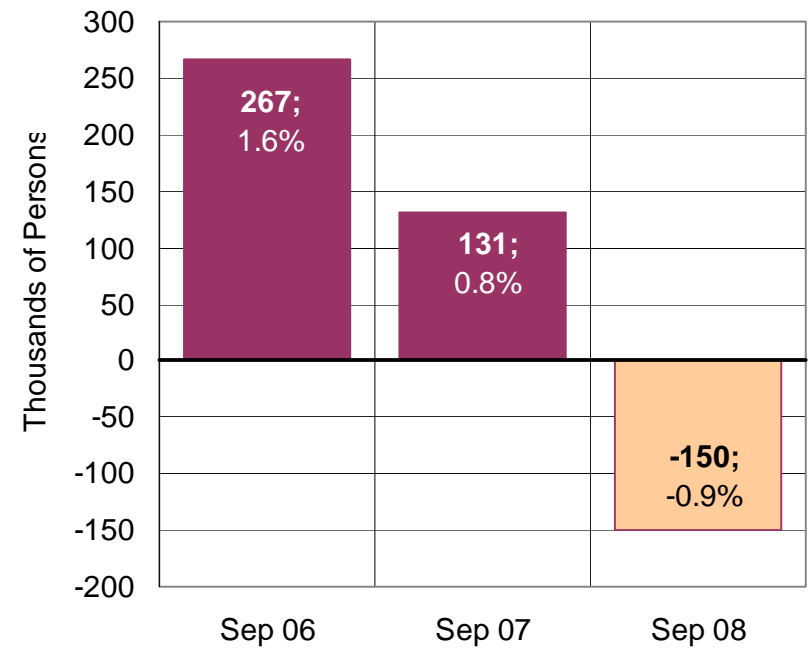


California Civilian Employment

**California Civilian Employment
Three-Year Trend**
September 2008; Seasonally Adjusted Data

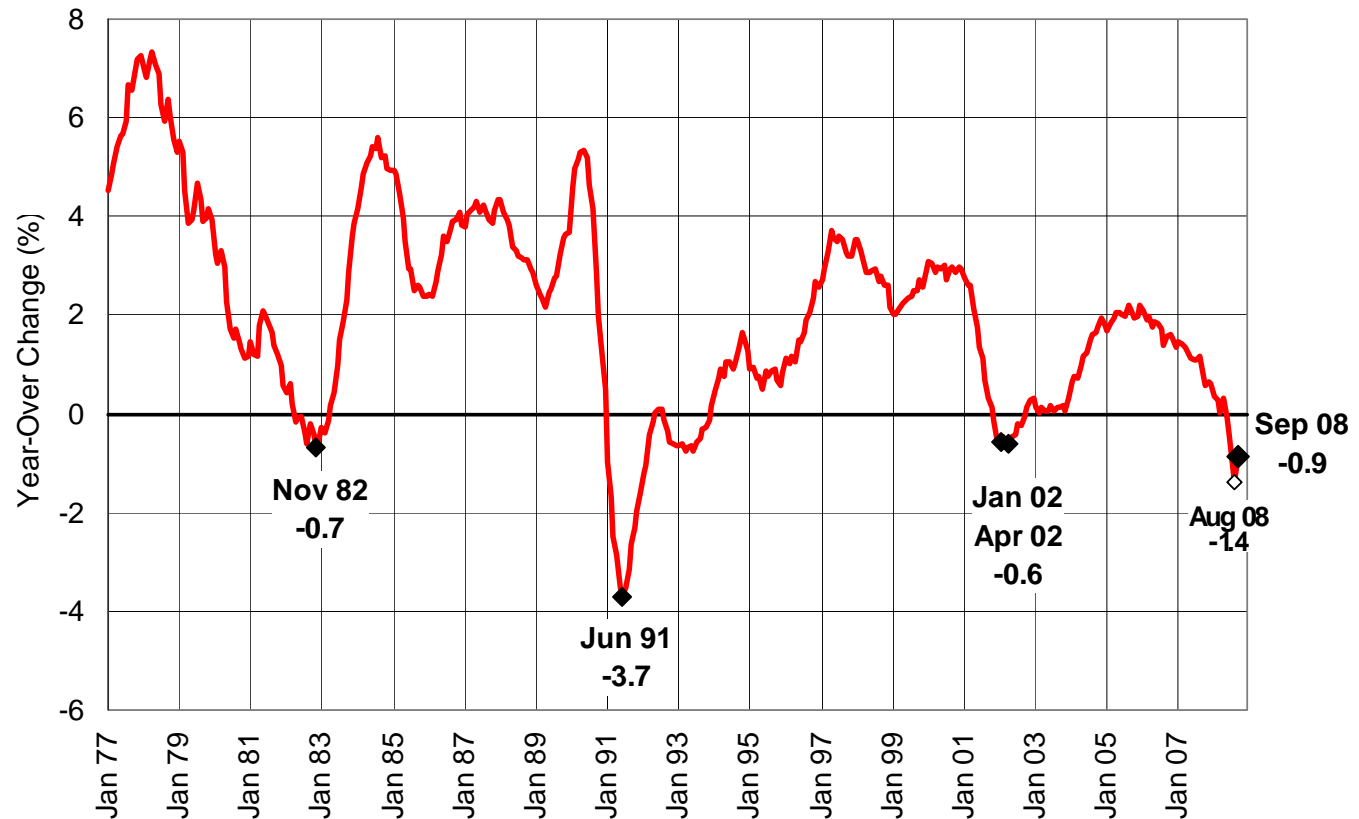


**Year-Over Changes in California
Civilian Employment**
September 2008; Seasonally Adjusted Data



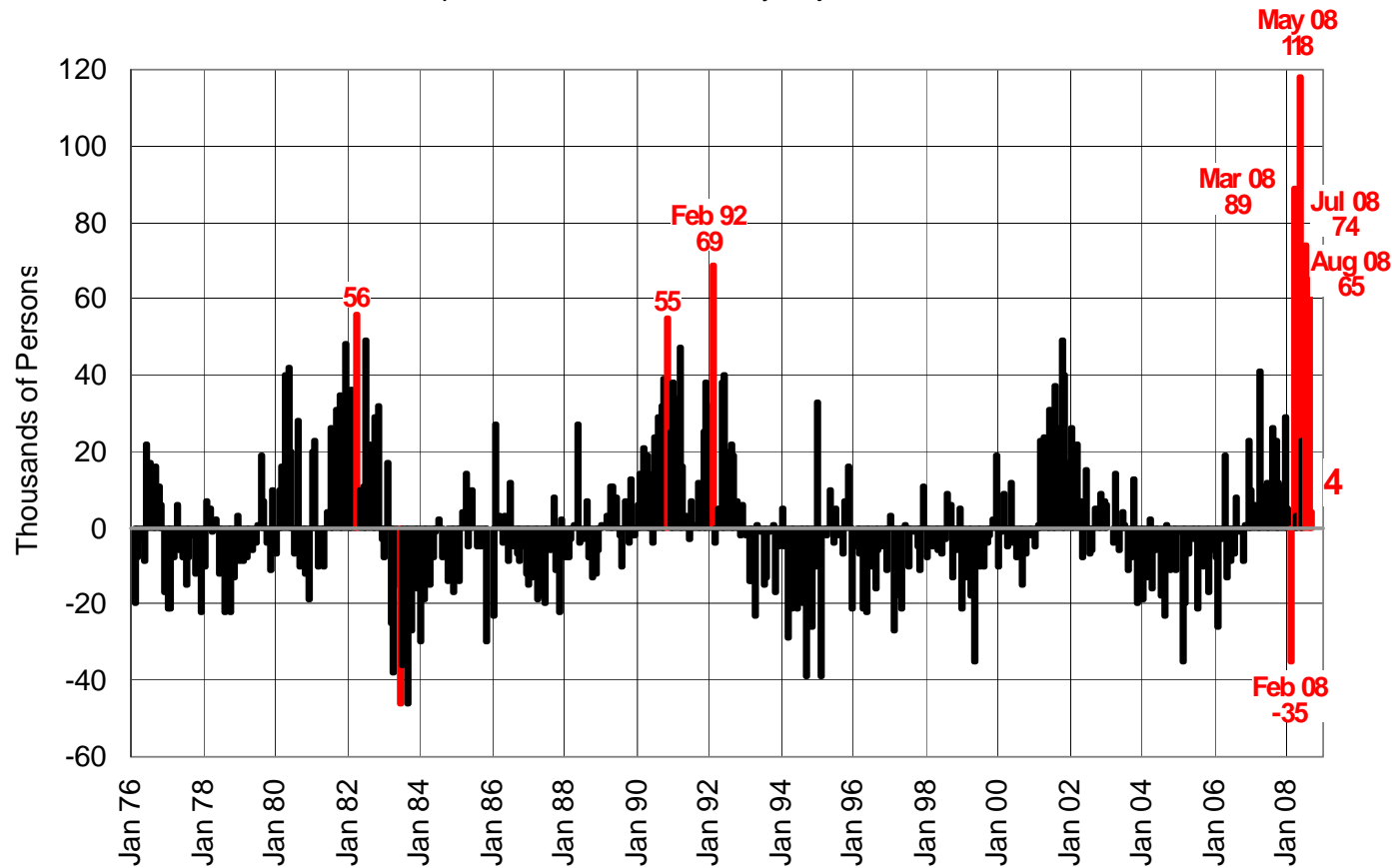
Year-Over Percentage Changes in California Employment Since 1977

September 2008; Seasonally Adjusted Data



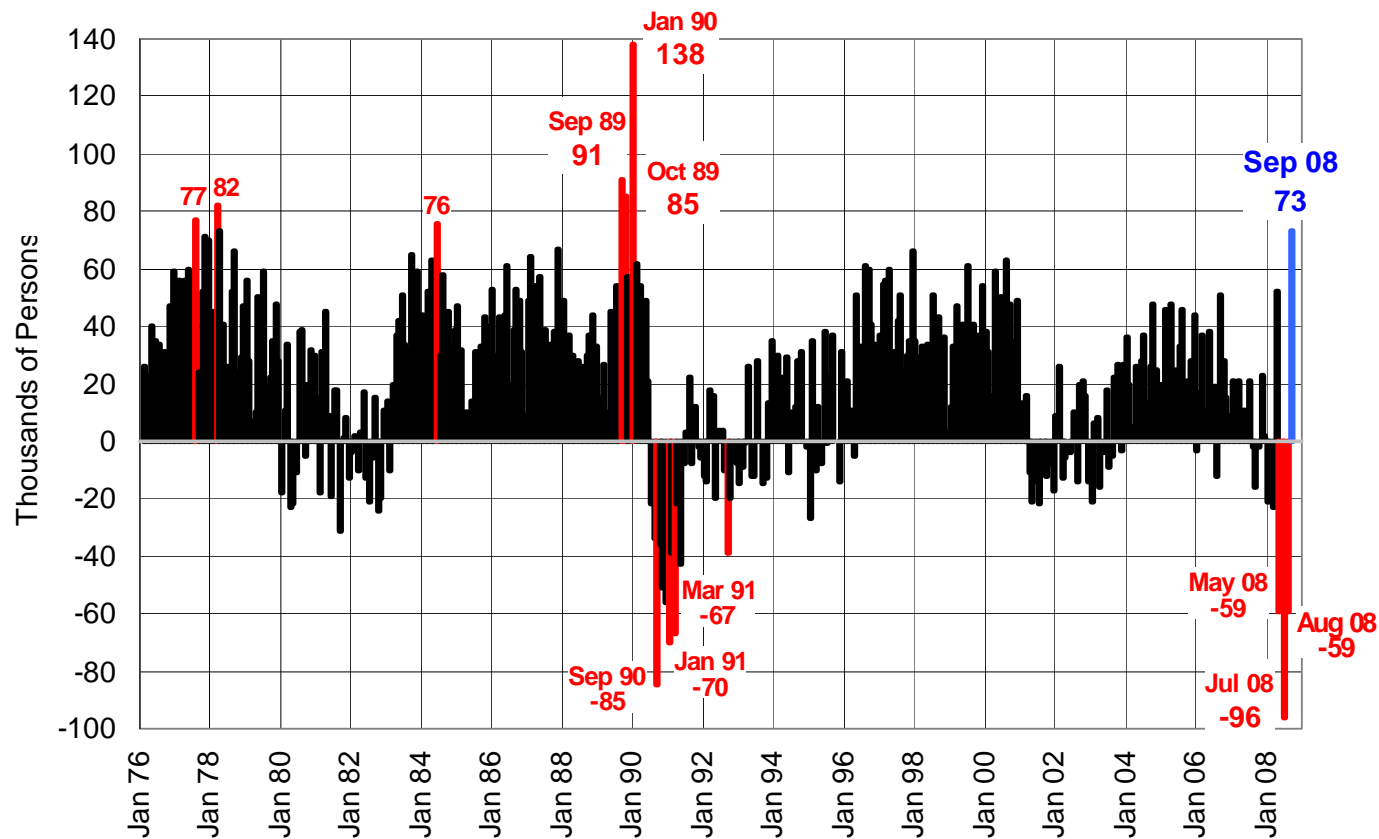
Month-Over Changes in California Unemployment Since 1976

September 2008; Seasonally Adjusted Data



Month-Over Changes in California Employment Since 1976

September 2008; Seasonally Adjusted Data



California Nonfarm Payrolls

California Nonfarm Employment

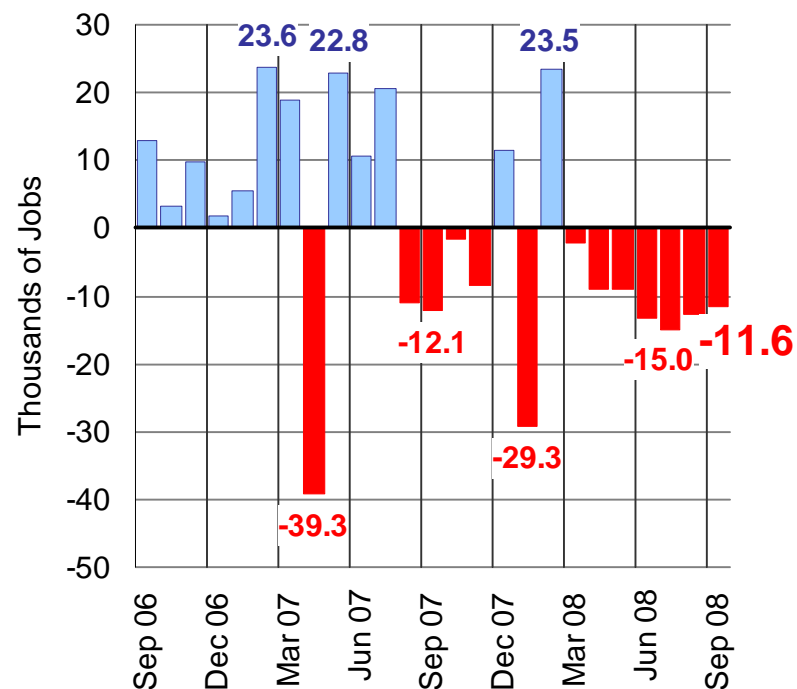
September 2005 - September 2008

Seasonally Adjusted Data

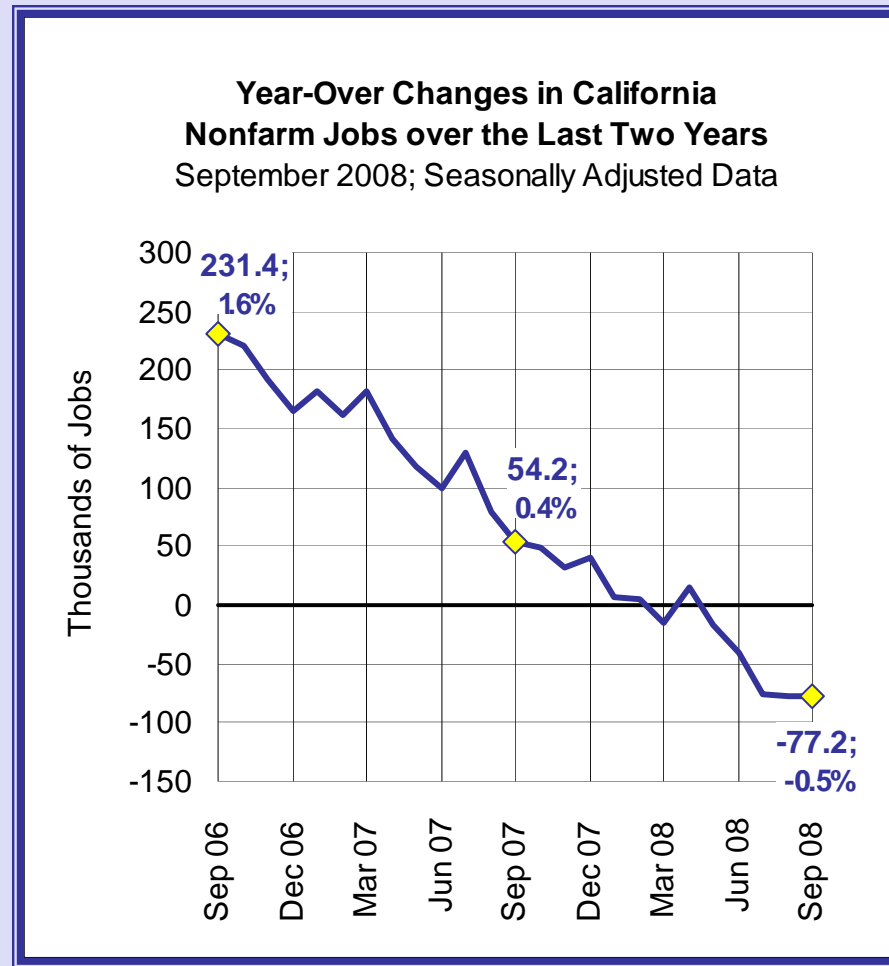


Month-Over Changes in California Nonfarm Jobs Over the Last Two Years

September 2008; Seasonally Adjusted Data



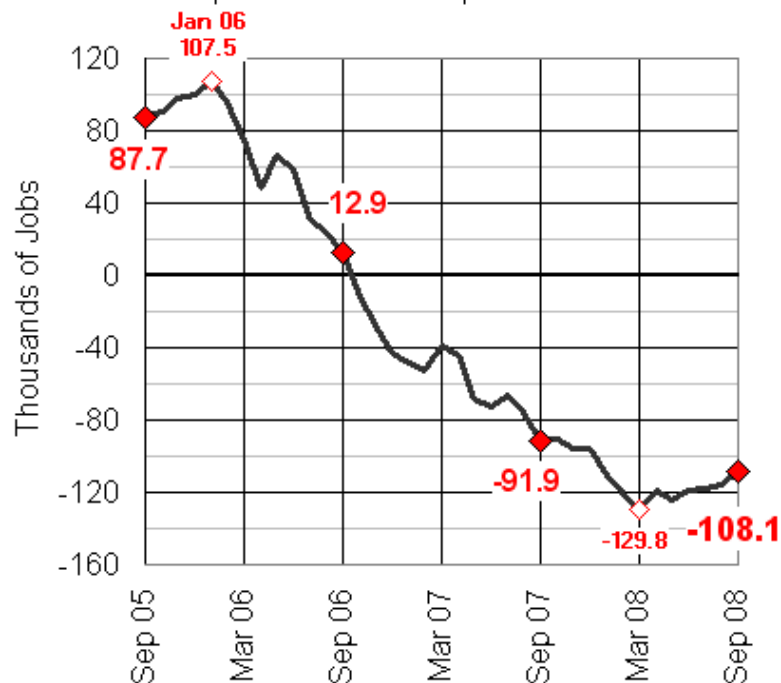
California Nonfarm Payrolls (Continued).



California's employment slowdown, although still centered in housing, is spilling into the larger economy

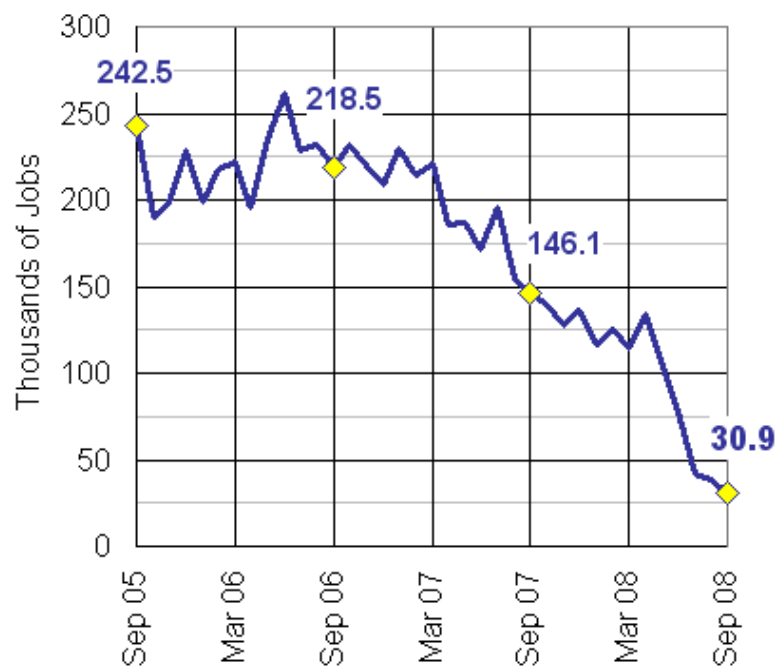
Year-Over Changes in Number of Construction and Financial Activities Jobs

September 2005 - September 2008



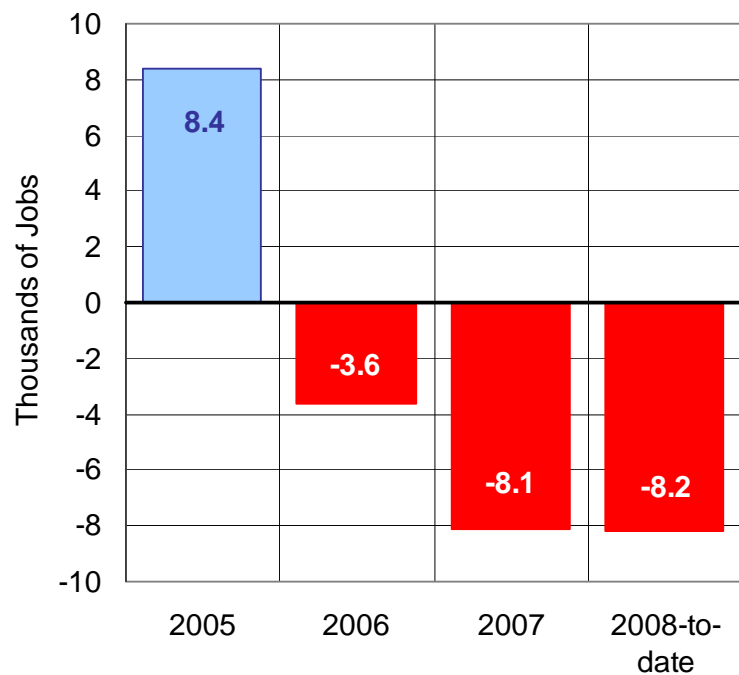
Year-Over Changes in Number of Total Nonfarm Jobs Excluding Construction and Financial Activities

September 2005 - September 2008

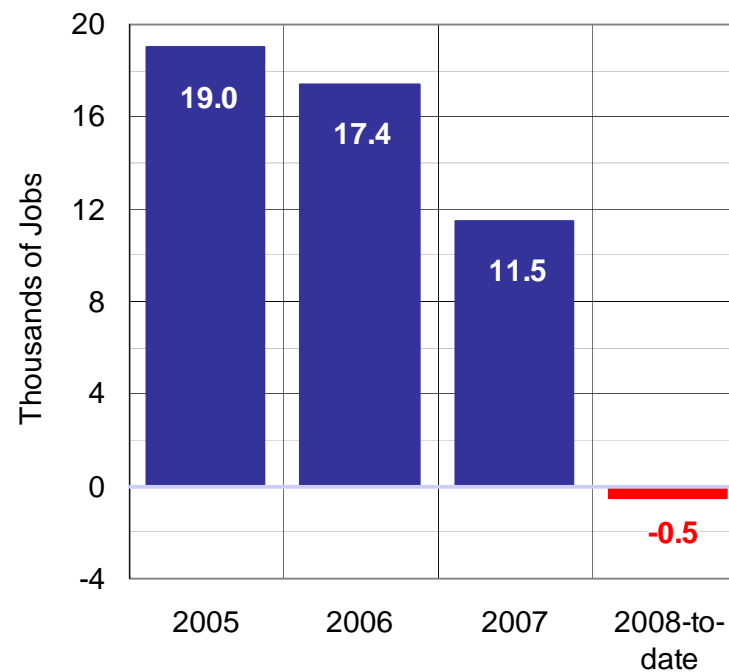


2008-to-Date

**Average Monthly Change in California
Construction and Financial Activities Jobs**
September 2008; Seasonally Adjusted Data

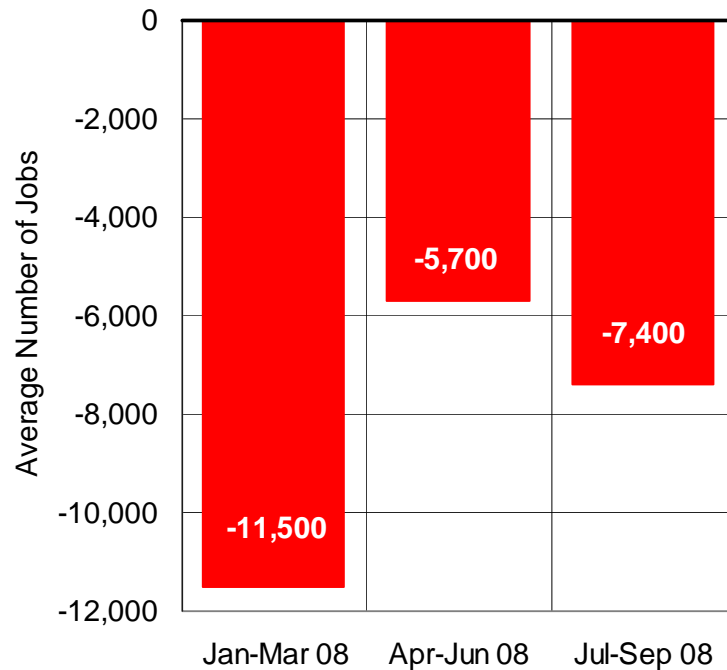


**Average Monthly Change in California
Nonfarm Jobs Excl. Construction and
Financial Activities**
September 2008; Seasonally Adjusted Data



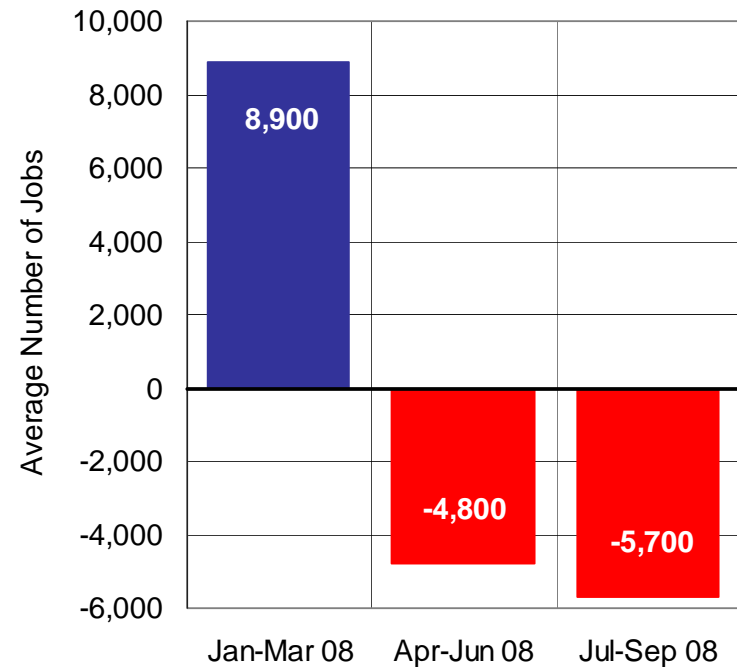
On Closer Inspection...

**Average Monthly Change in California
Construction and Financial Activities Jobs**
(Jan. - Sept. 2008; Seasonally Adjusted Data)



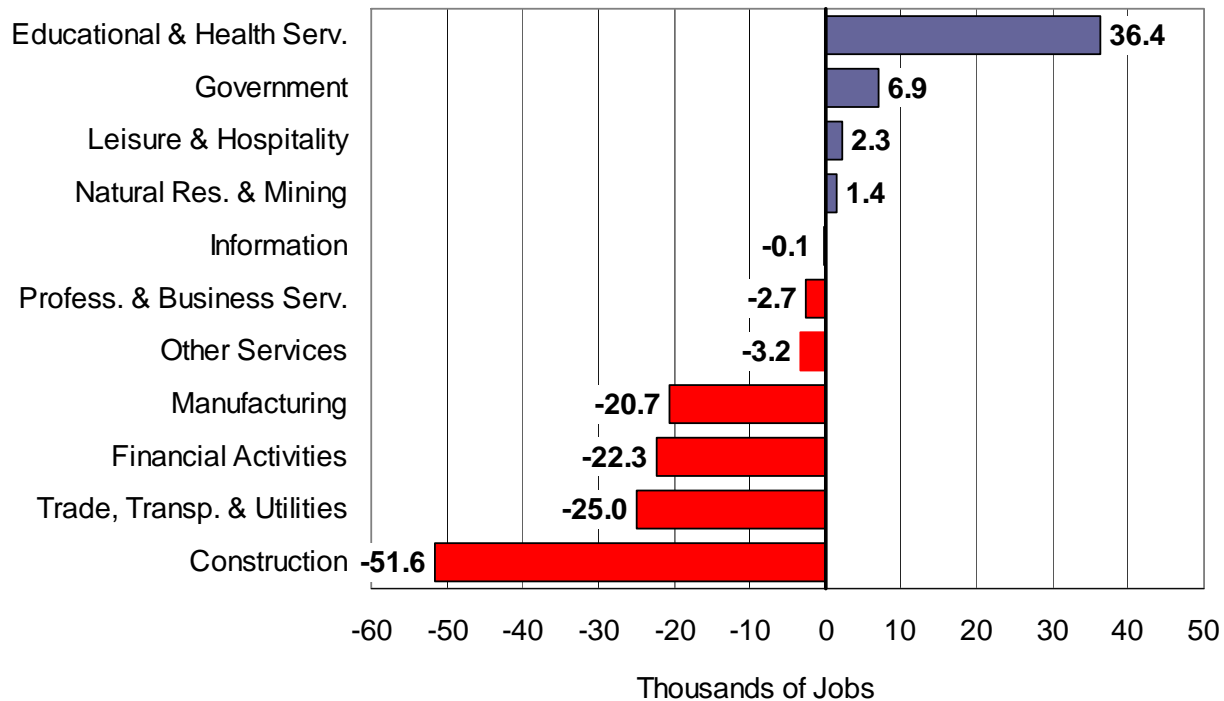
**Average Monthly Change in California
Nonfarm Jobs Excl. Construction and
Financial Activities**

(Jan. - Sept. 2008; Seasonally Adjusted Data)



California Industry Job Trends in 2008-to-Date

Year-to-Date Job Changes in California Industry Sectors,
(September 2008; Seasonally Adjusted Data)



California Industry Job Growth Trends During 2008-to-Date

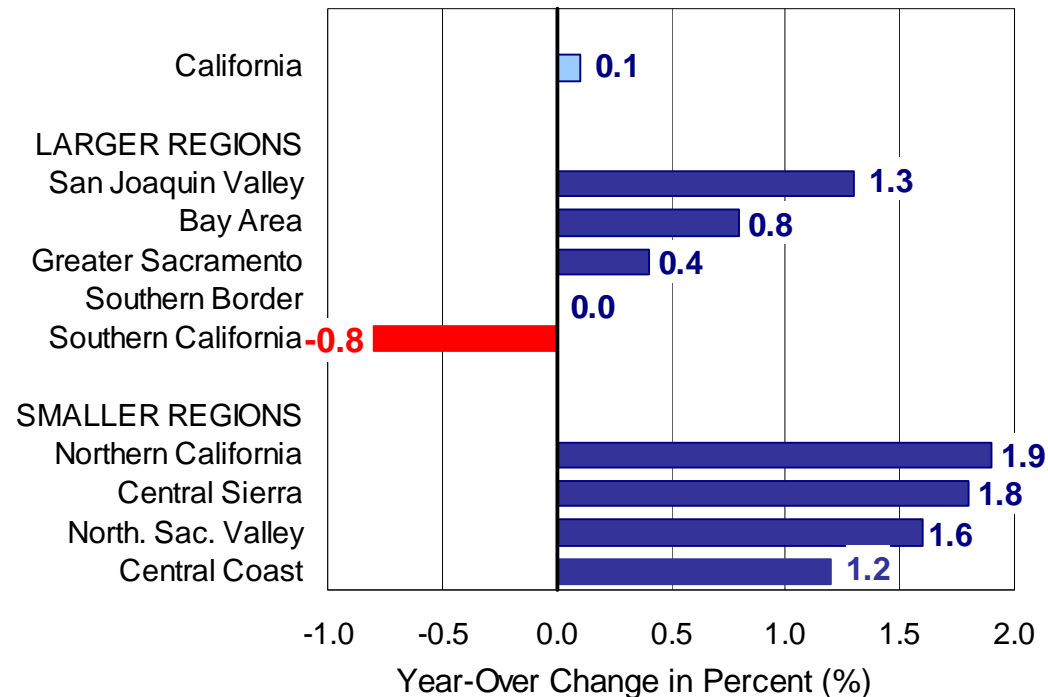
2008-to-Date Job Changes in California Nonfarm Employment and Major Industry Sectors: First Five Months and Last Four Months of 2008 Compared (September 2008; Seasonally Adjusted Data)

	January - May 2008		June - September 2008	
	<u>Change in</u> <u>Number</u>	<u>Change</u> <u>Per Month</u>	<u>Change in</u> <u>Number</u>	<u>Change</u> <u>Per Month</u>
Total Nonfarm	-25,900	-5,200	-52,700	-13,200
Natural Resources and Mining	1,400	300	0	0
Construction	-40,300	-8,100	-11,300	-2,800
Manufacturing	-10,400	-2,100	-10,300	-2,600
Trade, Transportation and Utilities	-3,600	-700	-21,400	-5,300
Information	-7,400	-1,500	7,300	1,800
Financial Activities	-11,100	-2,200	-11,200	-2,800
Professional and Business Services	4,800	1,000	-7,500	-1,900
Educational and Health Services	25,600	5,100	10,800	2,700
Leisure and Hospitality	3,300	700	-1,000	-300
Other Services	-2,600	-500	-600	-200
Government	14,400	2,900	-7,500	-1,900

Regional Job Growth Trends When Last We Spoke

Year-Over Percent Change in Nonfarm Employment in California Economic Regions

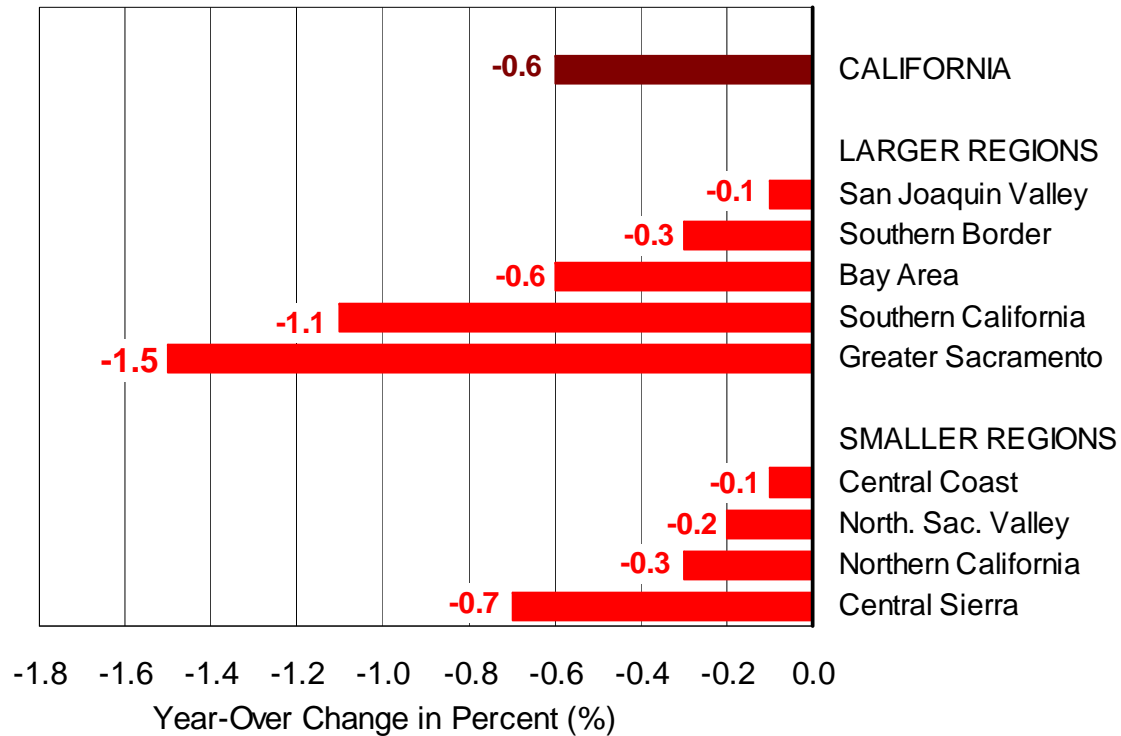
February 2008; Not Seasonally Adjusted Data



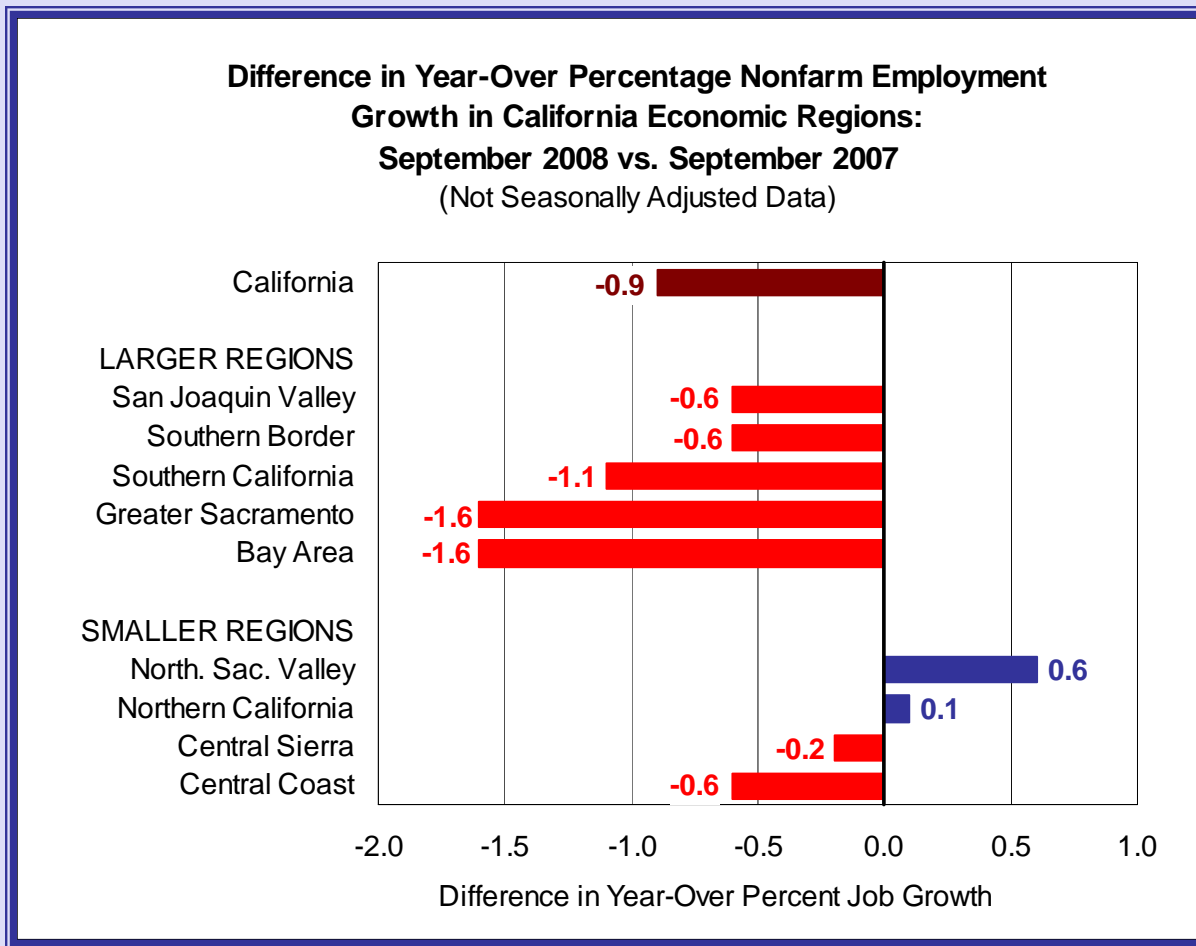
Regional Job Growth Trends in September 2008

Year-Over Percent Change in Nonfarm Employment in California Economic Regions

September 2008; Not Seasonally Adjusted Data



Regional Job Growth Trends in September 2008



California Nonfarm Payrolls

How does the current situation compare to past downturns?

